

# **AUDITOR'S REPORT OF THE AUDITOR-GENERAL TO THE LIMPOPO PROVINCIAL LEGISLATURE AND THE COUNCIL ON CAPRICORN DISTRICT MUNICIPALITY**

## **REPORT ON THE FINANCIAL STATEMENTS**

### **Introduction**

1. I was engaged to audit the accompanying financial statements of the municipality, which comprise the statement of financial position as at 30 June 2010, and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information, as set out on pages XXX to XXX.

### **Accounting Officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and in the manner required by the Municipal Finance Management Act of South Africa No. 56 of 2003 (MFMA). This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

### **Auditor-General's responsibility**

3. As required by section 188 of the Constitution of South Africa and section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), my responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the International Standards on Auditing and *General Notice 1570 of 2009* issued in *Government Gazette No. 32578 of 27 November 2009*. Because of the matters described in the Basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

### **Basis for disclaimer**

#### **Revenue**

4. The district municipality is a water authority in terms of section 84(1)(b) and 84(1)(d) of the Municipals Structures Act, 1998 (Act No. 117 of 1998). The municipality has appointed local municipalities falling within its jurisdiction as service providers in terms of Section 78 of the Municipals Systems Act, 2000 (Act No 32 of 2000).
5. The district municipality did not recognise water revenue for water services rendered on its behalf as there were no proper systems and controls in place to account for such revenue. I consequently could not confirm that all revenue inflows that should have been recorded have been recorded and disclosed in the financial statements. The municipality's records did not permit the application of alternative procedures regarding revenue.
6. Accordingly, I was not able to determine whether any adjustments might be necessary to the amounts shown in the financial statements for revenue, the surplus for the year or the accumulated surplus.

#### **Trade and other receivables**

7. The district municipality did not recognise accounts receivable for water services rendered on its behalf as there were no proper systems and controls in place to account for such receivable. I consequently could not confirm that all receivables that should have been recorded have been recorded and disclosed in the financial statements. The municipality's records did not permit the application of alternative procedures regarding debtors.
8. Accordingly, I was not able to determine whether any adjustments might be necessary to the amounts shown in the financial statements for impairments of accounts receivable, bad debts written off, the surplus for the year or the accumulated surplus.

#### **Value added tax (VAT)**

9. The district municipality did not recognise VAT on the water service revenue that should have been recorded, as there were no proper systems and controls in place to account for such balance. I consequently could not confirm whether the VAT that should have been recorded has been recorded and disclosed in the financial statements. The municipality's records did not permit the application of alternative procedures regarding VAT.

#### **Employee Cost**

10. During the preceding financial year ended 30 June 2009, adequate documentation was not provided for car allowances amounting to R9 717 503. My opinion on the financial statements for the period ended 30 June 2009 relating to the car allowance amount was modified accordingly. My opinion on the current period financial statements is also modified as adequate documentation could not be provided for the car allowance amounting to R12 251 044.

#### **Leave provision**

11. The long term leave provision to the amount of R11 453 678 as disclosed in the statement of financial position was not measured in terms of the International Accounting Standard (IAS) 19 *Employee benefits*. The standard requires measurement to be based on an actuarial valuation or the projected unit method. The district municipality had measured the balance based on actual leave days and basic salaries only. I consequently could not confirm whether the said balance has been correctly valued. The municipality's records did not permit the application of alternative procedures regarding non-current liabilities.

#### **Cash flow statement**

12. Presentation of a cash flow statement, summarising the entity's operating, investing and financing activities is required by Standard of Generally Recognised Accounting Practice, GRAP 2, *Cash flow statement*. An error was noted in the corresponding figures for the net cash flows from financing activities. The error arose as a result of the payment for the financial lease liability what was recorded as a cash inflow instead of a cash outflow. As a result, the net cash flows from financing activities and the cash and cash equivalents for the period ended 30 June 2009 in the cash flow statement are overstated by R5 075 309.

#### **Expenditure**

13. Contrary to the preceding financial year's service level agreements and current year council resolution, the district municipality has not recorded the commission payable to the local municipalities who have rendered water services on the district municipality's behalf.

14. I consequently could not confirm that all expenditure relating to the commission payable that should have been recorded have been recorded and disclosed in the financial statements. The municipality's records did not permit the application of alternative procedures regarding the expenditure.
15. Accordingly, I was not able to determine whether any adjustments might be necessary to the amounts shown in the financial statements for expenditure, the surplus for the year or the accumulated surplus.

#### **Property, Plant and Equipment**

16. Standards of Generally Recognised Accounting Practice, GRAP 17, *Property, plant and equipment* requires that assets acquired at a nil or nominal value should be recognised at fair value on initial recognition. As indicated in note 5.4 to the financial statements, a transfer of 49 assets was made from the Department of Environmental Affairs and Tourism to the district municipality in the current financial year. The assets were recorded at nominal values of R1 each which is in contravention of GRAP 17. The effect on property, plant and equipment and other classes of transactions contained in the financial statements could not be determined.

#### **Disclaimer of opinion**

Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

#### **Emphasis of matter**

I draw attention to the matters below. My opinion is not modified in respect of these matters:

#### **Irregular Expenditure**

17. As disclosed in the note 34 to the financial statements, irregular expenditure to an amount of R40 746 848 was incurred due non-compliance to the supply chain management regulations.

#### **Restatement of corresponding figures**

18. As disclosed in note 29 to the financial statements, corresponding figures for 30 June 2009 have been restated as a result of errors discovered during 2010 in the annual financial statements of the Capricorn District Municipality at, and for the year ended 30 June 2009

#### **Additional matters**

I draw attention to the matters below. My opinion is not modified in respect of these matters:

#### **Unaudited supplementary schedules**

19. The supplementary information set out on pages XXX to XXX does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

## **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

20. In terms of the PAA of South Africa and *General notice 1570 of 2009*, issued in *Government Gazette No. 32758 of 27 November 2009*, I include below my findings on the report on predetermined objectives, compliance with the following key laws and regulations and financial management (internal control).

### **Findings**

#### **Predetermined objectives**

21. Material findings on the report on predetermined objectives, as set out on pages XXX to XXX, are reported below:

#### **Non-compliance with regulatory and reporting requirements**

##### ***Report on predetermined objectives not received on time***

22. The reliability of the targets as set out on pages XX to XX of the annual report, could not be verified, since the information was not received in time for audit purposes.

#### **Compliance with laws and regulations**

##### **MFMA**

#### **Expenditure was incurred in contravention of or not in accordance with applicable legislation resulting in irregular expenditure**

23. Expenditure was not incurred in accordance with the requirements of the supply chain management policy of the municipality giving effect to such policy as set out in section 1 the definition of "irregular expenditure" paragraph (d) of the MFMA.

#### **Municipal Systems Act of South Africa, No 32 of 2000 (MSA)**

##### **Annual declarations not made by those charged with governance**

24. Contrary to section 7(a) of schedule 1 of the MSA, evidence of annual declarations of interest to be made by the councillors was not submitted to the audit.

#### **Municipal Structures Act of South Africa, No 117 of 1998**

##### **Functions and responsibilities of the district municipality**

25. Contrary to section 84(1) of the above act, the local municipalities performed the water function and not the district municipality. No ministerial approval was obtained to deviate from the provisions of the above act.

## **INTERNAL CONTROL**

26. I considered internal control relevant to my audit of the financial statements and the report on predetermined objectives as well as compliance with the MFMA, MSA and Municipal Structures Act, but not for the purpose of expressing an opinion on the effectiveness of internal control.

27. The matters reported below are limited to the significant deficiencies regarding the basis for disclaimer of opinion paragraph, the findings on the report on predetermined objectives and the findings on compliance with laws and regulations.

## **Leadership**

### *Oversight responsibility*

28. The accounting officer does not exercise oversight responsibility over reporting and compliance with laws and regulations and internal control.
29. Actions have not been taken to address material misstatements reported in the prior year's audit of financial statements.
30. The accounting officer does not evaluate whether management has implemented effective internal controls by gaining an understanding of how senior management has met its responsibilities.

### *Action to mitigate risks*

31. Actions are not taken to address risks relating to the achievement of complete and accurate financial and performance reporting.
32. External audit findings are not addressed.

## **Financial and performance management**

### *Quality, reliable annual financial statements*

33. The financial statements were subject to material amendments resulting from the audit.
34. The annual performance report was not submitted for auditing as per the legislated deadlines.

### *Adequate systems*

35. General information technology controls are not designed to maintain the integrity of the information systems and the security of the data.

## **Governance**

### *Internal audit*

36. Decreased focus on matters related to financial and performance reporting.

## OTHER REPORTS

### Investigations

#### Investigation in progress

37. An investigation is being conducted by a contracted firm to probe the manner in which the supply chain management process was applied by the district municipality. The investigation aims to establish whether any irregularities had taken place in the procurement of goods and services. The investigation was still ongoing at the reporting date.

*Auditor-General*

Polokwane

30 November 2010



AUDITOR-GENERAL  
SOUTH AFRICA

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